In the Supreme Court of the United States

OCTOBER TERM, 1965

No. 1207

ELMER J. BENES, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

In this case the Tax Court, in a lengthy opinion with detailed findings (App. 68a–116a),[1] resolved three issues against the petitioners. It held: (1) that petitioner Elmer Benes realized taxable income from the construction of a residence for him by the corporate petitioner which he controlled, and that the corporation understated its income by charging the expenses of such construction to other work it was doing; (2) that the individual petitioners (Elmer and his wife Frances) constructively received income from the corporation to the extent that the latter

[1] "App." refers to the appendix to the petitioners' brief in the court of appeals.

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deducted as salary payments to them amounts in excess of what it actually paid them; and (3) that all the petitioners had fraudulently understated their income and were liable for penalties therefor. The court of appeals affirmed *per curiam* "for the reasons set forth" in the Tax Court's opinion (Pet. 19). That decision is correct, and there is no occasion for further review of these primarily factual issues.

1. Petitioner Elmer Benes was the president and the owner of 500 of the 503 outstanding shares of the corporate petitioner (App. 73a–74a). The corporation constructed at a cost of approximately $173,000, a 25-room house for him (App. 76a, 92a), which he and his family occupied as their personal residence (App. 87a). Pursuant to Elmer Benes' instructions, the corporation charged on its books various costs incurred in the construction of his residence to other construction jobs it was then doing, although it did not bill its customers for those costs (App. 77a–78a). The corporation used the amounts thus charged off against the other jobs to reduce its gross income therefrom (App. 77a). During the portion of the taxable years involved that Benes occupied the house, he made no payments to the company either as rent or as a purchase price (App. 87a).

The Tax Court, on the basis of these and other facts (App. 76a–87a), concluded that the expenses the corporation incurred in building the house were intended to provide "a personal, private residence for the Company's president and chief stockholder, Elmer J. Benes," and that during the taxable years involved he did not intend to pay the company therefor (App.

100a, 102a). The court rejected the contention that the residence had been built as a "make-work" project to keep the company's labor force busy, stating that the "labor was engaged to build a residence for the Company's president rather than an asset for the Company" (App. 103a). Whether the corporation's construction of the house for Benes be viewed as payment of additional salary to the principal officer or as divideneds to the controlling stockholder, the value of such construction constituted taxable income to Benes. See the cases cited by the Tax Court, App. 104a.

2. The Tax Court, recognizing that the Commissioner had the burden of establishing fraud by "clear and convincing evidence," further found that the tax deficiencies reflected in the returns of the company and the individual petitioners were "due in major part to fraud with intent to evade tax," and that the Commissioner therefore had correctly imposed fraud penalties (App. 100a). In the case of the corporation, the court stated that "the manner in which these * * * residence costs were placed on the Company's books of account was such as to conceal their true character as personal expenses of an officer-stockholder," and that Benes, as a corporate officer, had lied to an Internal Revenue agent as to the cost of the house and the source of the funds used therefor (App. 113a). In the case of Benes individually, the court concluded that the "'fraudulent intent which actuated him in causing the corporation to understate its income through charging and deducting his personal items as corporate expense, spills over to infect

the joint returns which he and his wife filed. His omission to report the amounts expended for his benefit by his corporation was, we are convinced, done with a fraudulent intent to evade and defeat Federal income taxes which he knew to be due and owing" (App. 114a–115a). The court of appeals in effect adopted these findings as its own, and they fully support the ultimate conclusion that petitioners fraudulently concealed taxable income.

3. Benes' annual salary was $12,000 plus a percentage of the profits (App. 97a).[2] In 1947 the company credited him and deducted as a business expense, total salary of approximately $18,000 calculated in accordance with the above arrangement (App. 109a). Benes and his wife reported salary of only $8,900, apparently on the ground that this was all they actually received. The Tax Court sustained the Commissioner's determination that the difference between these two amounts constituted taxable income which the Beneses constructively had received in 1947. It stated (App. 110a):

> Since Elmer, in his position as president of the Company and with full power and authority, alone wrote the checks on the Company's bank account, and since the Company's cash position as far as this record shows was such as to permit the payment of the individual petitioners' full officer salaries as deducted by the Company, we must conclude that Elmer and Frances could have actually withdrawn and received the full amount of their salaries. They must be re-

[2] His wife, petitioner Frances Benes, was to receive $600 annually as secretary of the corporation (App. 98a).

garded, as the respondent has determined, as having constructively received the full amounts.

This conclusion was correct. A taxpayer on a cash basis is subject to taxation on income which he has the power to receive, even though he elects not to do so. *Corliss* v. *Bowers,* 281 U.S. 376. Benes had the power to direct the corporation to pay him and his wife the total amount of the salaries to which they were entitled; the corporation had funds available therefor. They constructively received the entire income due them in that year (*Ross* v. *Commissioner,* 169 F. 2d 483, 492, C.A. 1), even though he decided to leave a portion thereof with the corporation for its temporary use. *Branden* v. *Commissioner,* 3 BTA 231.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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